LIBRARY
SUPREME COURT, U. S.

Office-Supreme Court, U.S.
FILED
SEP 16 1963
JOHN F. DAVIS, CLERK

Supreme Court of the United States

No. 382

VAUGHAN B. CONNELLY, DEBTOR,
Petitioner

v.

CENTRAL STATES, SOUTHEAST AND SOUTHWEST AREAS PENSION FUND,
Respondent

Petition for a Writ of Certiorari to the United States Court of Appeals for the Fifth Circuit

BRIEF OF CENTRAL STATES, SOUTHEAST AND SOUTHWEST AREAS PENSION FUND IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

ROBERT C. WARD
1240 duPont Building
Miami, Florida — 33131
Attorney for Respondent

WARD & WARD
1240 duPont Building
Miami, Florida — 33131
Of Counsel

INDEX

	Page
INTRODUCTION	1
JURISDICTION	2
STATEMENT OF FACTS	3
QUESTIONS PRESENTED:	
1. An Unrecorded Instrument Modifying and Altering the Terms of a Recorded Instrument Cannot Affect a Bankrupt Estate Simply Because Both Instruments Prior to the Bankruptcy Proceedings Were Executed by a Party Subsequently Appointed in the Bankruptcy Proceedings as the Debtor in Possession for the Estate.	7
2. A Lien on Real Estate, the Title to Which is in a Bankrupt Estate Not Having Been Established or Proved, Cannot Be Valid.	8
3. The Status of a Lien on Realty, the Title to Which is in a Bankrupt Estate, Is Controlled by the State Recording Statutes as Interpreted by the Various State Courts Wherein Said Real Estate Is Located, and By the Restriction Contained in the Acts of Congress Relating to Bankruptcy	8
ARGUMENT:	
Question 1	11
Question 2	12
Question 3	16
CONCLUSION	17
CERTIFICATE OF SERVICE	

AUTHORITIES CITED

	Page
Bank of Douglas v. Neal (Ariz.) 247 Pac. 132	14
Chavis v. Gibbs (Va. 1956) 94 S.E.2d 195	9
City of Sanford v. Ashton (Fla.) 179 So. 765	15
Commercial Bk. of Ocala v. 1st Nat'l. Bk. (Fla.) 87 So. 315	14
Grace v. Hendricks (Fla.) 140 So. 790	14
Magnum Import Co. v. Coty (1923) 43 Sup.Ct. 531	2
O'Neill v. Cole (Va.) 72 S.E.2d 382	10
State ex rel. Squire v. Pejsa (Ohio) 72 N.E.2d 374	14
Stretch v. Murphy (Ore.) 112 P.2d 1018	14

Rule 19, Revised Rules Supreme Ct. of U. S.	8
11 U.S.C. 110	12
11 U.S.C. 47(c)	2
28 U.S.C. 1254(1)	2
Vol. 8, Code of Va. (1959 Replacement) Par. 55-59	10
Vol. 12, Permanent Ed., Words & Phrases, Deficiency Judgment	14

Supreme Court of the United States

No. _____

VAUGHAN B. CONNELLY, DEBTOR,
Petitioner

v.

CENTRAL STATES, SOUTHEAST AND SOUTHWEST AREAS PENSION FUND,
Respondent

Petition for a Writ of Certiorari to the United States Court of Appeals for the Fifth Circuit

BRIEF OF CENTRAL STATES, SOUTHEAST AND SOUTHWEST AREAS PENSION FUND IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

INTRODUCTION

For purposes of brevity, the Petitioner, Vaughan B. Connelly, Debtor, will be referred to as "Connelly"; the Respondent, Central States, Southeast and Southwest Areas Pension Fund, will be referred to as "Pension Fund"; and references to the Record shall be by the symbol "R".

JURISDICTION

The Petitioner Connelly has made application to this Court for a writ of certiorari to the United States Court of Appeals for the Fifth Circuit, directed to an opinion rendered by that court on March 29, 1963 in an appeal wherein Connelly was appellant and the Pension Fund was appellee.

The petition asserts jurisdiction in this Court under the provisions of 11 U.S.C. 47(c) and 28 U.S.C. 1254(1). After a complete reading of the petition, your Respondent fails to find any allegations or suggestions in compliance with Rule 19 of the Revised Rules of the Supreme Court of the United States (formerly Rule 38). There is no assertion that the decision of the Court of Appeals is in conflict with any other Court of Appeals' decision, or that the court has decided an important question of federal law which has not been settled by this Court and that should be settled by this Court, or that it has decided a federal question in conflict with a prior decision of this Court; nor has he presented any other grounds, as outlined in said Rule 19. The only remote indication given by the petition of compliance with Rule 19 is some general statements that the decision of the Court of Appeals has misinterpreted the applicable law of the State of Virginia. This point is discussed under the argument of your Respondent.

This Court, in discussing its jurisdiction in certiorari matters, state in **Magnum Import Co. v. Coty (1923) 262 U.S. 159, 67 Law. Ed. 922, 43 Sup.Ct. 531:**

"The jurisdiction to bring up cases by certiorari

> from Circuit Courts of Appeals was given for two purposes, first to secure uniformity of decision between those courts in the nine circuits, and second, to bring up cases involving questions of importance which it is in the public interest to have decided by this court of last resort. **The jurisdiction was not conferred upon this court merely to give the defeated party in the Circuit Court of Appeals another hearing.**" (emphasis supplied)

The petition herein demonstrates that Petitioner seeks nothing more than another hearing from this Court on matters clearly adjudicated by the Court of Appeals.

STATEMENT OF FACTS

In order that the Court can better understand the argument of your Respondent, we include in this brief a resume of the facts leading to the decision of the Court of Appeals. The facts are somewhat repetitious of those contained in the petition, but Respondent feels it is necessary in order to give a continuity to its argument.

In 1959, the Pension Fund loaned Connelly a total of $4,300,000. This loan was secured by a mortgage on the Everglades Hotel located in the City of Miami, Dade County, Florida. The Pension Fund, not being satisfied with the Hotel as the sole security for the loan, required additional collateral security to be placed by Connelly. By reason thereof, Connelly gave to the Pension Fund, as additional collateral security for the mortgage on the Everglades Hotel, an $800,000 deed of trust on vacant property located in Alexandria, Virginia. This is the property which is involved in this particular litigation.

In connection with the giving of the collateral security on the Virginia property and the giving of other collateral security, a loan and pledge agreement was entered into between Connelly and the Pension Fund (R 115 to 127). To evidence this $800,000 collateral pledge of the Virginia property, Connelly and his wife executed a deed of trust under Virginia law, which deed of trust was duly recorded among the public records of Virginia (R 108 to 114). The deed of trust contained the following statement:

> "The note secured hereby is given as collateral security for a larger indebtedness secured by real estate in Dade County, Florida, and the indebtedness hereby secured shall be considered paid in full at such time as the sum of $1,300,000 has been paid on the principal of the indebtedness in Dade County, Florida hereinabove mentioned." (R 109-110)

By reason of defaults in the primary mortgage on the Everglades Hotel, the Pension Fund instituted foreclosure proceedings on the Everglades Hotel in the United States District Court for the Southern District of Florida, Miami Division, which resulted in the entry of a final decree of forclosure on August 24, 1960 (R 1 through 15). The property was sold pursuant to the final decree and the Pension Fund was the successful purchaser; title to the property was delivered to the Pension Fund's nominee (R 16).

In August, 1960, Connelly had instituted proceedings first under Chapter XI of the Acts of Bankruptcy and later under Chapter XII of the Acts of Bankruptcy. In

February, 1961, Connelly filed a petition seeking to have all lien claimants establish the validity, priority and amount of thei lien (R 17) on certain property owned by Connelly, which was the subject matter of the bankruptcy proceedings.

The Pension Fund was served with an order to show cause requiring it to appear and present its claim to a lien on the Virginia property involved in this litigation. The Pension Fund filed its answer to the rule to show cause, setting up the final decree of foreclosure to establish the amount due it, and alleging that at the foreclosure sale it had bid $2,500,000 for the property, and alleging that by subtracting the $2,500,000 bid at the foreclosure sale from the amount due under the final decree, there still remained due the Pension Fund the sum of $2,179,257.70, plus interest and accrual. The Pension Fund claimed a third lien on the Virginia property by reason of the deed of trust given by Connelly to the Pension Fund to secure the funds due on the Everglades Hotel (R 42 to 45).

Connelly filed a reply to this answer of the Pension Fund wherein Connelly admitted the deed of trust, the recording thereof, and that said deed of trust granted to the Pension Fund a collateral lien of $800,000, but alleged that since the deed of trust stated that when the amount of $1,200,000 was paid on the Dade County, Florida mortgage, the Virginia mortgage was cancelled. Connelly claimed that by reason of the Pension Fund's bid of $2,500,000 at the foreclosure sale, this constituted payment sufficient to cancel the lien on the Virginia property (R 46-47).

Connelly also attempted to bring before the Referee in Bankruptcy the question of the Pension Fund's right to a deficiency decree in connection with the difference in the amount bid at the foreclosure sale and the amount still due under the final decree. The Referee entered his order on July 25, 1962 on the issues framed and first held, and rightly so, that he had no right to determine the question of a deficiency since the District Court had reserved jurisdiction on that matter (R 53 and final decree of foreclosure R 15).

The Referee found that the bid at the foreclosure sale of $2,500,000 satisfied the requirements of the deed of trust on the Virginia property and that by reason thereof, the lien of the Pension Fund on the Virginia property was cancelled and rendered null and void (R 52 to 54).

The Court will note that nowhere in the Referee's order did he find that the Pension Fund had failed to prove its lien on the Virginia property. To the contrary, the Referee's order is based upon the fact that there was a valid lien upon the property, but that the conditions of said deed of trust creating said lien had been satisfied and that on that basis, the lien should be cancelled.

A petition for review was taken by the Pension Fund. Connelly sought no petition of review from the decision of the Referee with regard to his lack of jurisdiction to determine a deficiency or to determine the question of values of the Dade County, Florida property. On review, the District Court reversed the Referee and simply held that the bid of the Pension Fund at the foreclosure sale was not a payment under the terms of the Virginia

deed of trust, which would authorize the court to cancel the lien of the Pension Fund on the Virginia property. The court held that the pursuing by the mortgagee of his rights against one of the several parcels of land given as security after default by the mortgagor could not in any way be construed as barring him from pursuing the other security so long as mortgagee had not realized the full amount due him (R 129 to 134).

There is no mention in the District Court's opinion about the question of a deficiency decree. From this decision, Connelly prosecuted an appeal to the United States Court of Appeals for the Fifth Circuit and on March 29, 1963 that court affirmed the District Court, which opinion appears as Appendix A to the petition for writ of certiorari.

QUESTIONS PRESENTED

The petition states that there are three questions involved which should give rise to this Court's exercising its discretionary power in issuing a writ of certiorari. The questions presented are as follows:

1. AN UNRECORDED INSTRUMENT MODIFYING AND ALTERING THE TERMS OF A RECORDED INSTRUMENT CANNOT AFFECT A BANKRUPT ESTATE SIMPLY BECAUSE BOTH INSTRUMENTS PRIOR TO THE BANKRUPTCY PROCEEDINGS WERE EXECUTED BY A PARTY SUBSEQUENTLY APPOINTED IN THE BANKRUPTCY PROCEEDINGS

AS THE DEBTOR IN POSSESSION FOR THE ESTATE.

2. A LIEN ON REAL ESTATE, THE TITLE TO WHICH IS IN A BANKRUPT ESTATE, NOT HAVING BEEN ESTABLISHED OR PROVED, CANNOT BE VALID.

3. THE STATUS OF A LIEN ON REALTY, THE TITLE TO WHICH IS IN A BANKRUPT ESTATE, IS CONTROLLED BY THE STATE RECORDING STATUTES AS INTERPRETED BY THE VARIOUS STATE COURTS WHEREIN SAID REAL REAL ESTATE IS LOCATED, AND BY THE RESTRICTION CONTAINED IN THE ACTS OF CONGRESS RELATING TO BANKRUPTCY.

The Pension Fund will respond to each of the questions raised for a two-fold purpose, first to show that there is no substantial question raised, as required by Rule 19 of the Revised Supreme Court Rules, and second to the merits of each question to demonstrate the correctness of the decision of the Court of Appeals.

ARGUMENT.

QUESTION 1. AN UNRECORDED INSTRUMENT MODIFYING AND ALTERING THE TERMS OF A RECORDED INSTRUMENT CANNOT AFFECT A BANKRUPT ESTATE SIMPLY BECAUSE BOTH INSTRUMENTS PRIOR TO THE BANKRUPTCY PROCEED-

INGS WERE EXECUTED BY A PARTY SUBSEQUENTLY APPOINTED IN THE BANKRUPTCY PROCEEDINGS AS THE DEBTOR IN POSSESSION FOR THE ESTATE.

Under this question, Connelly takes issue with the opinion of the Court of Appeals which found that he, as debtor in possession, was bound by the unrecorded loan and pledge agreement. As can be noted by previous statements in this brief, this was not the real issue before the Court of Appeals, but it did comment about Connelly's argument on this point. The reasoning of the court in reaching this conclusion is simply one of interpretation of the law of Virginia concerning constructive notice. Nowhere does the opinion of the Court of Appeals attempt to hold that a trustee appointed in bankruptcy proceedings, or a debtor in possession, can be bound by unrecorded instruments between the debtor and a third person. The holding of the Court of Appeals was that the statement contained in the recorded deed of trust, that said deed was collateral security for a larger loan on property in Dade County, Florida, was sufficient under the Virginia constructive notice law, and also Florida law, to put a prudent person on notice concerning other unrecorded agreements existing between the parties on the same subject. This is clearly in line with the law of Virginia and the law of Florida. In the case of **Chavis v. Gibbs, 198 Va. 379, 94 S.E.2d 195** (1956, S.Ct. of Appeals of Va.) the Virginia court, in construing the recording statutes and notice given thereby, stated:

> "It is an established rule in Virginia that where a party purchases an estate which is subject to the right of another and that right is shown by

the chain of title paper **the purchaser is charged with notice** of all that the title paper or papers to which they refer may disclose upon complete examination, citing Effinger v. Hall, 81 Va. 94; Burwell v. Fauber, 21 Grat. 446; Virginia Iron Coal and Coke Co. v. Roberts, 103 Va. 661, 49 S.E. 984, and authorities cited therein (emphasis supplied)."

Also in the case of **O'Neill v. Cole, 194 Va. 50, 72 S.E. 2d 382**, cited by the Court of Appeals, the court said:

> "The means of knowledge are equivalent to actual knowledge and knowledge of facts sufficient to suggest inquiry which, if made, would lead to knowledge of the facts in question is sufficient to charge one with notice of the latter facts."

In Volume 8, Code of Virginia 1950 Replacement 55-59 titled "How Deeds of Trust Construed, etc. * * * 1. The deed shall be construed as given to secure the performance of **each of the covenants entered into by the grantor** as well as the payment of the primary obligation (emphasis supplied)."

There is nothing in the opinion of the Court of Appeals that is in any way a radical departure from the precept of the bankruptcy law. The holding with regard to the binding effect of the loan and pledge agreement on Connolly, as debtor in possession, is merely the following by the Court of Appeals of the constructive notice law of Virginia and nothing more.

The point with regard to the binding effect of the loan and pledge agreement is really dicta. The sole question for determination by the Court of Appeals was whether or not the $2,500,000 bid at the foreclosure sale was a payment which would satisfy the conditions stated in the deed of trust. Your Respondent does not find that the Petitioner contends that the decision on this point was incorrect.

QUESTION 2. A LIEN ON REAL ESTATE, THE TITLE TO WHICH IS IN A BANKRUPT ESTATE NOT HAVING BEEN ESTABLISHED OR PROVED, CANNOT BE VALID.

This question borders on the ridiculous. There was no finding by the Referee in Bankruptcy, the District Court or the Court of Appeals that the deed of trust of the Pension Fund on this Virginia property was not proven. To the contrary, the validity of the deed of trust was admitted by Connelly in his reply to the original answer to the order to show cause to the Referee in Bankruptcy (R 46). If the lien of the deed of trust was not proven, then how could the Referee have found that the conditions of the deed had been satisfied and ordered said deed of trust cancelled of record as having been fully satisfied?

If Connelly felt the Pension Fund failed to establish its lien, then he should have sought review of that point in the District Court. When he did not, then the decision on that point is final (R 129).

Leaving that point, we find that the deed of trust was received in evidence without objection and was

identified by Connelly. The amount still remains due on the original mortgage given by Connelly to the Pension Fund was established by the simple arithmetical calculation of subtracting $2,500,000 from the amount stated in the final decree of foreclosure. The final decree was in evidence and is part of this record (R 1).

QUESTION 3. THE STATUS OF A LIEN ON REALTY, THE TITLE TO WHICH IS IN A BANKRUPT ESTATE, IS CONTROLLED BY THE STATE RECORDING STATUTES AS INTERPRETED BY THE VARIOUS STATE COURTS WHEREIN SAID REAL ESTATE IS LOCATED, AND BY THE RESTRICTION CONTAINED IN THE ACTS OF CONGRESS RELATING TO BANKRUPTCY.

A part of the answer to this question already has been discussed under your Respondent's argument of Question 1. It is respectfully submitted that the Virginia statutes and opinions of the Virginia courts amply sustain the Court of Appeals' construction of the recording statue of Virginia and the notice to be implied therefrom.

Petitioner asserts that he does not fall within the two categories covered by the Virginia recording statutes. The Virginia statute speaks of prospective purchasers and future encumbrancers. Under some theory not readily apparent from the argument of Petitioner, Connelly takes the position that he, as a trustee or debtor in possession, is not a prospective purchaser or a future encumbrancer. Section 70 of the Bankruptcy Act, 11 U.S.C. 110, is abundantly clear that the title of a trustee

or debtor in possession is equivalent, as stated in Section 3 thereof, to a creditor of the bankrupt who claims a lien by legal or equitable proceedings as of the date of bankruptcy. There is no question that the deed of trust given by Connelly to the Pension Fund on the Virginia property was dated and recorded prior to the institution of any bankruptcy proceedings by Connelly. As debtor in possession under the terms of Section 70 of the Act, Connelly must be classified as a future encumbrancer under the terms of the Virginia recording statute.

Connelly, as debtor in possession, stands in the same position in regard to the prior recorded deed of trust as any other subsequent lien creditor. He would take with the same notice, under the Virginia recording statute, as any other future encumbrancer.

ON THE QUESTION OF DEFICIENCY: The Petitioner has again attempted, as he did in the Court of Appeals, to throw confusion into this cause by raising the question of the right of the Pension Fund to a deficiency decree and the effect that it may have upon the rights of your Respondent in connection with its lien on the Virginia property involved in this litigation.

As was stated by the Court of Appeals, Connelly did not raise this question on petition for review from the order of the Referee in Bankruptcy; therefore, it was not a proper subject to be raised on appeal.

The opinion of the Court of Appeals, after reaching the conclusion that the matter was not properly before it, did give Connelly the benefit of its comments on this question. The Court of Appeals held, as did the District

Court, that the question of a deficiency could not become involved in the proceedings until after the creditor had exhausted his security. This is obviously a correct principle of law. By its very definition, a deficiency decree is a personal judgment entered against the signers of the promissory note after the holder of the note has exhausted, by sale or other proceedings, all of the security that was pledged for the payment of the note. See: **Grace v. Hendricks (Fla.) 140 So. 790; Commercial Bank of Ocala v. First National Bank (Fla.) 87 So. 315; Bank of Douglas v. Neal (Ariz.) 247 Pac. 132, 134; State ex rel. Squire v. Pejsa (Ohio) 72 N.E.2d 374; Stretch v. Murphy (Ore.) 112 P.2d 1018; Vol. 12, Permanent Edition, Words and Phrases, Deficiency Judgment.**

Your Respondent has no argument with the Petitioner's abstract theory of law that the awarding of deficiency decrees is within the sound discretion of the court. This is established by Florida Statute 702.06, but this would not allow a court to cancel the lien on one of several parcels of land given to secure a mortgage indebtedness when the sale of the other parcels has not produced sufficient funds to pay the amount of the indebtedness due.

The question of the value of the property involved could have some effect on the court in exercising its sound judicial discretion in determining whether or not it will grant a judgment against the makers of the obligation, but certainly this discretion would not allow a court to cancel the specific lien on property given by the mortgagor to secure the loan.

It is only logical that this question of discretion of

the court would not come into play until after all of the security given for the obligation has been exhausted. If this is not true, then the court would be changing the contract of the parties.

In his argument, the Petitioner makes the following statement:

> "The Opinion below fails to apply the legal doctrine of operation of the discharge from a lien of one of several parcels of real estate given as security for the repayment of an indebtedness, where the value of one parcel (which has been foreclosed) is sufficient to discharge the total obligation owed. Hence, if the mortgagee redeems one of several parcels, he discharges from the lien the remaining properties." (Pages 19-20 of Connelly's petition herein.)

Petitioner cites no authority to support such a legal doctrine. It is respectfully submitted there is none and that the contrary is true. See: **City of Sanford v. Ashton (Fla. 1938), 179 So. 765.**

The Petitioner states that the doctrine of which he speaks is recognized in Virginia and he cites §55-66.1 of 8 Code of Virginia as authority. A reading of said section of the Virginia code demonstrates the fallacy of this entire argument. This section merely authorizes a lienor, if he so desires for valuable consideration, to release a portion of property secured by a mortgage without being worried such partial release might be construed as a discharge of the whole. This statute is absolutely of no solace or substantiation to the argument of the Petitioner.

CONCLUSION

It is respectfully submitted that the Petitioner has wholly failed to show any basis for the granting of certiorari in this cause. The decision of the Court of Appeals in no way confuses the law and is not in conflict with the opinion of any other Circuit or of this Court, nor is it in conflict with any applicable law of Virginia or of Florida.

The only real question before the Referee in Bankruptcy, the United States District Court and the United States Court of Appeals for the Fifth Circuit was whether or not the bid of $2,500,000 by the Pension Fund at the foreclosure sale was payment on the mortgage, which would result in a cancellation of such deed of trust.

The Referee answered this question in the affirmative; the District Court and the Court of Appeals both held that a bid at a foreclosure sale was not payment as prescribed in the deed of trust.

Respondent does not find any statement in the Petition for Writ of Certiorari which attempts to point out that the decision on this point by the Court of Appeals was in error or in conflict with any other decision.

The argument made by the Petitioner is an argument against a portion of the opinion which is mere dicta and was not the real point in issue.

Putting aside the question that portions of the opinion of the Court of Appeals were not dicta, the Petitioner still has not pointed out any error in the state-

merits made by the Court of Appeals in applying the Bankruptcy Act, the laws of the State of Virginia and the laws of the State of Florida to the question involved, which would comply with Rule 19 of the Revised Supreme Court Rules.

It is respectfully submitted that certiorari should be denied.

Respectfully submitted,

ROBERT C. WARD
1240 duPont Building
Miami, Florida — 33131
Attorney for Respondent

WARD & WARD
1240 duPont Building
Miami, Florida — 33131
Of Counsel

CERTIFICATE OF SERVICE

I HEREBY CERTIFY that a copy of the foregoing brief has been served on Mr. Irving M. Wolff, Attorney for Petitioner, 1204 Biscayne Building, Miami, Florida, 33131, by depositing same in a United States post office, with first class postage prepaid, addressed to such counsel at the address indicated, this 14th day of September, 1963.

Robert C. Ward